

Message Text

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SUBJ: ECONOMIC ALERT REPORT

REF: A. STATE 180067, B. STATE 155681

FOLLOWING IS RESPONSE TO REFTEL QUESTIONS.

A. MAJOR ECONOMIC PROBLEMS

THIS QUESTION MUST BE PUT WITHIN THE CONTEXT OF A GENERAL IMPROVEMENT IN THE FISCAL, MONETARY, AND INTERNATIONAL TRADE AND FINANCE PERFORMANCE OF THE URUGUAY GOVERNMENT OVER THE PAST THREE YEARS. THE PROJECTED FISCAL DEFICIT FOR 1977 IS MINIMAL (10 PERCENT) AND REFLECTS MAJOR IMPROVEMENT OVER RECENT YEARS. A GAIN IN INTERNATIONAL RESERVES EQUALING LAST YEAR'S \$113 MILLION IS PREDICTED AGAIN THIS YEAR ON THE BASIS OF CONTINUING HEALTHY EXPORTS AND THE FOREIGN DEBT PROFILE IS CONSIDERED MANAGEABLE. INFLATION IS THE CURRENT SHORT-TERM PROBLEM; POLICY FOR THE PRO- DUCTIVE SECTORS IS A CONTINUING PROBLEM IN THE MEDIUM TERM. IN- FLATION HAS BEEN BROUGHT DOWN TO ABOUT 40 PERCENT LAST YEAR BUT PREDICTIONS ARE WELL ABOVE THAT FOR 1977. THIS ACCENTUATES THE POLITICAL/ECONOMIC BITE OF FALLING REAL INCOMES. OVER THE NEXT FEW YEARS, THE GOVERNMENT WILL HAVE TO DEAL WITH THE DISIN-
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CENTIVES ITS CURRENT POLICIES HAVE CREATED TO BASIC CATTLE PROJECTION AND IN SOME CROP PRODUCTION IF OUTPUT IS TO BE MAINTAINED EVEN AT CURRENT LEVELS. SIMILARLY, IT FACES A PERIOD OF READJUSTMENT OF INDUSTRY TO A PLANNED LOWERING OF URUGUAY'S EXTREMELY HIGH PROTECTIONIST BARRIERS. INDUSTRY IS FIGHTING EVEN INITIAL STEPS IN THIS DIRECTION. NONE OF THESE ARE CURRENTLY CRISIS-LEVEL PROBLEMS, BUT CONTINUING DEVELOPMENTAL ISSUES.

CURRENT BILATERAL PROBLEMS WITH THE U.S. INCLUDE OUTSTANDING COUNTERVAILING DUTY ACTIONS UNDER INVESTIGATION BY TREASURY. THE SYSTEM AFFECTING ALL THREE HAS BEEN FOUND BY LEGAL DEFINITION TO PROVIDE A SUBSIDY ACCORDING TO PRELIMINARY DECISION ANNOUNCED BY TREASURY. HOWEVER, SINCE THE GOVERNMENT INCLUDES THE WEIGHT OF EXPORT SUBSIDIES AMONG ITS FISCAL PROBLEMS AND HAD ALREADY BEGUN TO PHASE THEM OUT, THE MATTER HAS NOT TO DATE BECOME AN ACTIVE IRRITANT IN OUR BILATERAL RELATIONS. MORE SUBSTANTIAL IS THE MATTER OF U.S. ACTION ON POSSIBLE URUGUAYAN REQUESTS FOR FINANCING IN THE INTERNATIONAL FINANCIAL INSTITUTIONS. POSSIBLE U.S. USE OF ITS VOTE IN THESE INSTITUTIONS TO BRING ADDED LEVERAGE OT ITS CAMPAIGN FOR IMPROVED HUMAN RIGHTS PERFORMANCE BY THE URUGUAYAN MILITARY IS CENTRAL TO OUR RELATIONS. WE UNDERSTAND THE GOU WILL SOON RISK SEEKING FUND FOR SPECIAL OPERATIONS (FSO) FINANCING IN THE INTER-AMERICAN DEVELOPMENT BANK (IDB), OVER WHICH WE HAVE AN EFFECTIVE VETO. IN THE CASE OF OTHER REQUESTS FOR NORMAL DEVELOPMENT FINANCING FROM EITHER THE IDB OR WORLD BANK, WE CAN CHOOSE TO VOTE NO OR ABSTAIN. DOING EITHER WHEN THE LOAN IS NEVERTHELESS FINALLY APPROVED HAS A POLITICAL EFFECT THRUH IT DOES NOT DENY FINANCING; VOTING AGAINST THE LOAN WITH OTHERS TO DENY THE FINANCING HAS A DEVELOPMENTAL EFFECT OF A HIGHER DIMENSION. USE OF OUR VOTE SHOULD BE SYNCHRONIZED TO BRING MAXIMUM ADVANTAGE IN OUR EFFORT TO IMPROVE GOU PERFORMANCE IN HUMAN RIGHTS. LIMITED OFFICIAL USE

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AS FOR URUGUAYAN DOMESTIC ECONOMIC PROBLEMS WHICH MIGHT LEAD TO MAJOR BILATERAL OR MULTILATERAL CONFRONTATIONS, THE MISSION SEES NONE ON THE HORIZON. THERE ARE POTENTIAL PROBLEMS WITH THE LOCAL MEAT INSPECTION SERVICE RELATIVE TO SHIPMENTS TO THE U.S., BUT THERE IS TIME FOR THIS TO BE RESOLVED BEFORE THE NEXT SHIPMENT.

B. OUTLOOK FOR THE NEXT TWELVE MONTHS

THERE IS NOTHING VISIBLE IN THE URUGUAYAN ECONOMIC SITUATION SUGGESTING THAT ANY MAJOR UNFAVORABLE TURN OF EVENTS IS LIKELY. CHANGES IN THE GOVERNMENT EXPECTED WITHIN THE NEXT 12 MONTHS COULD LEAD EITHER TO IMPROVED OR TO DECLINING POLITICAL STABILITY. ANY ABRUPT MOVE AGAINST INFLATION COULD LEAD TO A CONTRACTION IN THE ECONOMY. THE EMBASSY CANNOT NOW PREDICT THESE RESULTS BUT NEITHER DOES IT HAVE ANY REASON TO BE PESSIMISTIC. IN ANY EVENT, RESERVES ARE ADEQUATE TO COVER SHORT-TERM DIFFICULTIES IN THE BALANCE OF PAYMENTS SHOULD THEY OCCUR. HUMAN RIGHTS MOVEMENT IS HARD TO PREDICT BUT COULD HAPPEN AS EARLY AS ASSISTANT SECRETARY TODMAN'S VISIT OF AUGUST 17-19. ON THE OTHER HAND, THE FOLLOWING IS THE CURRENTLY PROJECTED LIST OF REQUESTS FROM THE IFIS EXPECTED TO COME FROM THE GOU: THE PASO SEVERINO WATER SUPPLY LOAN WILL PROBABLY BE REQUESTED

FROM IDB ORDINARY CAPITAL FUNDS, ALTHOUGH THIS IS STILL NOT OFFICIAL (SEE STATE 155681). THE PROPOSED ANIMAL SANITATION LOAN (\$20 MILLION) HAS BEEN REQUESTED FROM IDB FSO FUNDS AND UNLESS THERE IS SOME CHANGE, THIS WILL BRING UP THE QUESTION OF USE OF OUR EFFECTIVE VETO. THE WORLD BANK WILL BE PREPARING AN AGRICULTURAL SECTOR LOAN (LIVESTOCK AND DAIRY), A HUMAN RESOURCES AND TECHNOLOGY LOAN, AND A POWER SYSTEM DISTRIBUTION LOAN DURING 1977/78. EACH OF THESE WILL HAVE TO BE CONSIDERED IN LIGHT OF HUMAN RIGHTS PROGRESS IN URUGUAY.

C. CRITICAL POINTS

HUMAN RIGHTS AND OUR IFI LEVERAGE ON UPCOMING LOANS WILL DICTATE THE CRITICAL POINTS CALLING FOR A U.S. POLICY RESPONSE DURING THE LIMITED OFFICIAL USE

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COMING YEAR. OTHERWISE, WE CANNOT NOW PREDICT SUBSTANTIAL LIKE-LIHOOD THAT ECONOMIC PROBLEMS WOULD DEVELOP OF SUCH MAGNITUDE THAT THE U.S. WOULD BE REQUIRED TO DEAL WITH THEM BILATERALLY OR EVEN MULTILATERALLY.
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